

This letter discusses sales of prescription drugs by servicemen. See 86 Ill. Adm. Code Part 140. (This is a GIL.)

May 9, 2007

Dear Xxxxx:

This letter is in response to your letter dated September 19, 2006, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.ILTAX.com to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

I am writing on behalf of ABC. We are a Pharmacy that provides prescriptions to Long Term Care Facilities. We are an institutional pharmacy and do not service any retail customers. I am writing for a legal opinion to see if our company is tax exempt under the Service Occupation Act [sic]. I read the General Information Letter posted on the website and although it clearly defines how a retail pharmacy should respond, the language is vague for non-retail pharmacies such as ours.

We have several issues. First, we are collecting from either a third party payer, such as an insurance company or Medicare/Medicade [sic]. Do we apply the tax to these orders and if so, how? Second, does tax apply to co-pays that are paid for by the resident's responsible party? Finally, we do sell directly to Long Term Care facilities for their house drugs and supplies. Is this considered taxable since they are providing it to the residents as part of the monthly fee's [sic] or a Medicare per diem that they are receiving.

As we are just beginning our services, we want to make sure that we are correctly accounting for our potential (if any) tax liability. If we are tax exempt, how do we go about applying for a certificate that states this.

I can be reached if you have any questions.

DEPARTMENT'S RESPONSE

Pharmacists who sell prescription drugs to customers are considered to be servicemen under the Service Occupation Tax Act.

Servicemen may calculate their tax base in one of four ways: (1) separately stated selling price; (2) 50% of the entire bill; (3) Service Occupation Tax on the cost price if they are registered de minimis servicemen; or, (4) Use Tax on the cost price if the servicemen are de minimis and are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use the second method where they will use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of the sales of service. Upon selling their product, they are required to collect the corresponding Service Use Tax from their customers. See 86 Ill. Adm. Code 140.106.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See 86 Ill. Adm. Code 140.101(f). This class of registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to sales of service. Servicemen that incur Service Occupation Tax collect the Service Use Tax from their customers. They remit the tax to the Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers. See 86 Ill. Adm. Code 140.108.

The final method of determining tax liability may be used by de minimis servicemen not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). Such de minimis servicemen may pay Use Tax to their suppliers or may self assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. Those servicemen are not authorized to collect "tax" from their service customers because they, not their customers, incur the tax liability. Those servicemen are also not liable for Service Occupation Tax. It should be noted that servicemen do not have the option of determining whether they are de minimis using a transaction-by-transaction basis. See 86 Ill. Adm. Code 140.109.

You have indicated that you sell prescription drugs to insurance companies, Medicare/Medicaid, purchasers who pay co-pays, and long term care facilities who provide the drugs to residents as part of the resident's monthly fee or a Medicare per diem. We do not have enough information about how these sales are transacted to respond specifically regarding their taxability, however, we hope the following information is helpful.

In general, sales made to Medicare and Medicaid are exempt from tax as sales to a government body so long as the exemption is properly documented through provision of an active exemption identification number “(E” number). See 86 Ill. Adm. Code 130.2080(a). While no tax may be due on payments made directly to vendors by Medicare or Medicaid, tax is due upon any portion of the bill paid by individuals or private insurance companies not covered by Medicare and Medicaid. This means when Medicare directly pays 80% of the medical bill and the remaining 20% is billed to the patient or his insurance company, assuming proper documentation of the exemption, the 80% is tax exempt as a governmental payment while the 20% is taxable. In the case of an unregistered de minimis serviceman, (see the final method above), they may take a pass through of the exemption when selling to Medicare or Medicaid. Such servicemen will still owe Use Tax on the portion of the cost billed to the patient. See 86 Ill. Adm. Code 140.108(a)(2)(A) and 86 Ill. Adm. Code 140.108(a)(2)(B).

Some health care organizations (e.g. hospitals) that make application to the Department are determined to be exclusively organized and operated for charitable purposes. These organizations receive an “E” number. Organizations that have secured tax exemption identification numbers from the Department are exempt from tax when purchasing tangible personal property for use in furtherance of organizational purposes, and vendors do not incur tax on such sales. See 86 Ill. Adm. Code 130.2005 and 130.2007.

If tangible personal property is not sold for use or consumption, but rather, for resale, the seller may accept a Certificate of Resale from the purchaser. No tax is imposed on a sale of property purchased for resale. Illinois law requires a Certificate of Resale to contain the information set out in 86 Ill. Adm. Code 130.1405(b). An example of a sale for resale might be if you sell prescription drugs to a “for profit” long term care facility, and the long term care facility sells them to their residents as part of the residents’ monthly fee. Again, unregistered de minimis servicemen may not give a certificate of resale. They must pay the Use Tax to their suppliers.

Please note that there is also an exemption for prescription and non prescription medicines and drugs sold for use by a person receiving medical assistance under Article 5 of the Illinois Public Aid Code who reside in a licensed long-term care facility, as defined in the Nursing Home Care Act. See 35 ILCS 115/3-5(13).

If you require additional information, please visit our website at www.ILTAX.com or contact the Department’s Taxpayer Information Division at (217) 782-3336. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Martha P. Mote
Associate Counsel

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